INDEX

	Page
Opinions below	1
Jurisdiction	1
Question presented	2
Statute and regulations involved	3
Statement	3
Summary of argument	8
Argument:	
I. The entire value of the property covered by the power of appointment should be included in the decedent's gross estate	15
A. The appointees actually succeeded to the interests appointed to them under the exercise of the power; their failure to renounce the appointment precludes their contention that the property did not "pass" under the power	18
B. Where, as here, the exercise of the power is effective to disturb the flow of benefits, there is a passing of all the property under the power	42
II. Even applying New York law, all of the property must be included within decedent's gross estate except one small share appointed outright to the widow	50
Conclusion	60
Appendix	61

CITATIONS

Cases:	
Arnold v. *Southern Pine Lumber Co.*, 58 Tex. Civ. App. 186	27
Boyce v. *Waller*, 9 Dana 478	27
Brooks Settlement Trusts, In re (1939) Ch. 993	28
Brotherhood v. *Pinkston*, 293 U. S. 96	59
Burnet v. *Harmel*, 287 U. S. 103	30
Canda, Re, 197 App. Div. 597	51
Chapman, Re, 133 App. Div. 337	51
Chauncey, Re, 102 Misc. 378	54
Clapp v. *Ingraham*, 126 Mass. 200	25
Commissioner v. *State Street Trust Co.*, 124 F. 2d 948	59

Cases—Continued. Page

Cooksey, Re, 182 N. Y. 92 ..... 43, 51, 52
Cutting v. *Cutting*, 86 N. Y. 522 24
Delano, Re, 176 N. Y. 486, affirmed *sub nom. Chanler* v. *Kelsey*, 205 U. S. 466 53
Detroit Bank v. *United States*, 317 U. S. 329 23
Dows, Re, 167 N. Y. 227, affirmed *sub nom. Orr* v. *Gilman*, 183 U. S. 278 ..... 43, 51, 52
Duryea, Re, 277 N. Y. 310 52
Foster, Re, 144 Misc. 622 56
Freeman's Estate (No. 1), 35 Pa. Super. Ct. 185 49
Graves v. *Schmidlapp*, 315 U. S. 657 24
Grinnell v. *Commissioner*, 70 F. 2d 705 37
Helvering v. *Clifford*, 309 U. S. 331 33
Helvering v. *Fitch*, 309 U. S. 149 60
Helvering v. *Grinnell*, 294 U. S. 153 ..... 11, 12, 27, 30, 34, 35, 43
Helvering v. *Hallock*, 309 U. S. 106 32
Helvering v. *Leonard*, 310 U. S. 80 60
Helvering v. *Safe Deposit Co.*, 316 U. S. 56 ..... 11, 25, 38
Hill v. *Treasurer & Receiver General*, 229 Mass. 474 26
Humes v. *United States*, 276 U. S. 487 59
King, Re, 217 N. Y. 358 ..... 51, 53
Lansing, Re, 182 N. Y. 238 ..... 27, 30, 34, 35, 43, 51
Lee v. *Commissioner*, 57 F. 2d 399 37
Legg's Estate v. *Commissioner*, 114 F. 2d 760 ..... 41, 48, 52
Lewis v. *Rothensies* (C. C. A. 3d), decided Sept. 1, 1943 41
Lichtenstein, Re, 177 Misc. 320 52
Lowndes, Re, 60 Misc. 506 ..... 51, 52
Lyeth v. *Hoey*, 305 U. S. 188 30
Maddock v. *Haines*, 88 F. 2d 350 56
Manning v. *Board of Tax Commissioners*, 46 R. I. 400 32
Minot v. *Treasurer & Receiver General*, 207 Mass. 588 32
Montague v. *State*, 163 Wis. 58 32
Morgan v. *Commissioner*, 309 U. S. 78 ..... 11, 13, 30
Pearce v. *Commissioner*, 315 U. S. 543 60
Potter's Estate, 13 Pa. Dist. & Co. R. 667 49
Power v. *Power*, 296 Ill. 611 56
Reynolds v. *Commissioner*, 42 B. T. A. 145 40
Robinette v. *Helvering*, 318 U. S. 184 ..... 59, 60
Rogers, Re, 71 App. Div. 461, affirmed, 172 N. Y. 617 51
Rogers, Re, 168 Misc. 633 19
Rothensies v. *Fidelity-Philadelphia Trust Co.*, 112 F. 2d 758 ..... 41, 48, 52
Rynear, Re, 130 Misc. 804 51
St. Matthews Bank v. *De Charette*, 259 Ky. 802 27
Slosson, Re, 216 N. Y. 79 52

Cases—Continued. Page

State v. *Brooks*, 181 Minn. 262, further hearing, 183 Minn. 251 ... 32
Sullivan v. *Straus*, 161 Pa. 145 ... 56
Taylor, Re, 209 App. Div. 299, affirmed, 239 N. Y. 582 ... 53
United States v. *Field*, 255 U. S. 257 ... 24, 25
Vanderbilt, Re, 50 App. Div. 246, affirmed, 163 N. Y. 597 ... 54
Vanderbilt, Re, 281 N. Y. 297, affirmed *sub nom. Whitney* v. *Tax Commission*, 309 U. S. 530 ... 53
Vaughan v. *Vandersteegen*, 2 Drew. 165 ... 28
Wachovia Trust Co. v. *Doughton*, 272 U. S. 567 ... 24
Warren, Re, 62 Misc. 444 ... 51
Wear v. *Commissioner*, 65 F. 2d 665 ... 37
Weissmann, Re, 137 Misc. 113, affirmed, 232 App. Div. 698 ... 57
Wienholz, Re, 94 Misc. 55 ... 56

Statutes:
Internal Revenue Code, Sec. 811 (U. S. C., Title 26, Sec. 811) ... 27
New York Laws (1897), c. 284, Sec. 220 ... 31
Revenue Act of 1918, c. 18, 40 Stat. 1057, Sec. 402 ... 20
Revenue Act of 1926, c. 27, 44 Stat. 9, Sec. 302, as amended ... 15, 61
Revenue Act of 1942, c. 619, 56 Stat. 798, Sec. 403 ... 27, 42

Miscellaneous:
59 A. L. R. 1520 ... 25
97 A. L. R. 1071 ... 25
121 A. L. R. 804 ... 25
Eisenstein, *Powers of Appointment and Estate Taxes: I*, 52 Yale L. J. 296, 322 (1943) ... 32
Farwell, *Powers* (2d ed., 1893) 275–278 ... 28
Griswold, *Powers of Appointment and the Federal Estate Tax*, 52 Harv. L. Rev. 929, 935, fn. 27 (1939) ... 34, 41
H. Rep. No. 767, 65th Cong., 2d Sess., pp. 21–22 (1939–1 Cum. Bull. (Part 2) 86, 101) ... 20
3 Page on *Wills* (Lifetime Ed.), Sec. 1070 ... 56
1 Paul, *Federal Estate and Gift Taxation* (1942) pp. 449–451 ... 28
Restatement of Property, Proposed Final Draft No. 2, pp. 140, 151–155 ... 27
3 Restatement, Property (1940):
Pp. 1810–1812 ... 21, 28
Pp. 1855–1857 ... 24
Sec. 327, Comment b ... 26
Sec. 329, Comment d ... 26
Sec. 369 ... 26
Illustrations 2 and 3 ... 27
Second Caveat ... 48

Miscellaneous—Continued.

	Page
3 Tiffany, Real Property (3d ed.):	
Sec. 680	24
Sec. 713	24
Treasury Regulations 37 (1919 ed.), Art. 30	33
Treasury Regulations 37 (1921 ed.), Art. 30	33
Treasury Regulations 63 (1922 ed.), Art. 25	33
Treasury Regulations 68 (1924 ed.), Art. 24	33
Treasury Regulations 70 (1926 ed), Art. 24	33
Treasury Regulations 80 (1937 ed.):	
Art. 10	57
Art. 24	15, 62

In the Supreme Court of the United States

OCTOBER TERM, 1943

No. 66

ESTATE OF HENRY H. ROGERS, DECEASED, ADRIAN H. LARKIN, ALBERT STICKNEY, AND CENTRAL HANOVER BANK AND TRUST COMPANY, EXECUTORS, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The memorandum opinion of the Board of Tax Appeals (R. 25–27) is unreported. The opinions in the Circuit Court of Appeals (R. 113–122) are reported at 135 F. 2d 35.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered April 19, 1943 (R. 122). Petition

for a writ of certiorari was filed May 20, 1943, and was granted June 21, 1943 (R. 123). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Under his father's will, the decedent, Henry H. Rogers, enjoyed the income of certain trust property for life and possessed a general testamentary power of appointment with respect to it. In default of appointment the property at decedent's death would have gone to his widow, son, and daughter outright in equal shares. Decedent exercised the power by will, appointing (1) one-third of the property outright to a grandson, (2) 6.667 percent of a one-third share outright to his widow and the balance of this share in trust to pay the income to her, and upon her remarriage to pay over one-half of the corpus, and upon her death, the balance of it, to his daughter, if then living, and (3) 6.667 percent of the remaining third to the daughter outright, and the balance in trust to pay the income to her for life, and at her death to pay over the corpus to her then surviving issue. The question is whether the value of the property appointed outright to the widow and the daughter and the value of their respective interests as beneficiaries of the income of the trusts should be included in the

decedent's gross estate under Section 302 (f) of the Revenue Act of 1926, as amended.[1]

STATUTE AND REGULATIONS INVOLVED

The pertinent statute and regulations are set forth in the Appendix, *infra*, pp. 61–63.

STATEMENT

The stipulated facts, which were adopted by the Board of Tax Appeals (R. 25), may be summarized as follows:

The decedent, Henry H. Rogers, died July 25, 1935, a resident of New York. The petitioners are the duly qualified executors under his will, letters testamentary having been granted to them by the Surrogate's Court of Suffolk County, New York, on October 28, 1935. (R. 46.) Under the will of his father, Henry H. Rogers, Sr., who died a resident of New York in 1909, decedent was given the income from certain property which was placed in trust. One-half of the corpus was to be distributed to him when he became 40 years

[1] It is not disputed that the one-third share appointed to the grandson and the interests appointed to follow the interests of the widow and daughter, respectively, as beneficiaries of the income of the trusts fall within the decedent's gross estate (R. 50). In referring hereafter to the trust interests or trust estates of the widow and daughter we refer only to their interests as income beneficiaries during the period of the trusts, unless the text states otherwise. Thus, we do not include by these expressions the contingent interest of the daughter in the corpus of the widow's trust, which petitioners do not deny must be included in the gross estate.

of age; the balance was to remain in trust until decedent's death and was then to be paid over to such persons or corporations and in such manner as decedent in his last will might appoint, or, in the absence of appointment, to such persons as should then constitute his heirs at law as in the case of the inheritance of real property under the laws of New York. (R. 46–47, 56–57.) Decedent became 40 years of age in 1919 and half of the corpus of the trust was then paid over to him (R. 47). The balance remained in trust until decedent's death in 1935. Its value at the date of death was $8,428,949.60 (R. 49).

Decedent left surviving him his widow, two children by a former wife—Henry H. Rogers III and Millicent Rogers Balcom—and three grandchildren—Peter Salm and two others, who were the children of Millicent Rogers Balcom (R. 48). Decedent's heirs at law, as in the case of the inheritance of real property under the laws of New York, within the provisions of his father's will, were his widow, Henry H. Rogers III, and Millicent Rogers Balcom. In default of appointment, they would have taken the property subject to the power of appointment outright in equal shares. (R. 49.)

By his will decedent exercised the power of appointment in the following manner: By the Twelfth Article of his will he directed that the property subject to the power of appointment be

held in trust and divided into three equal shares. (1) The trustees were to pay the income from one share to his widow, and upon her death were to pay the principal to the then surviving issue, if any, of his marriage with her (in fact, there was no issue), and otherwise to decedent's "other issue surviving her, except Henry, per stirpes and not per capita."[2] In the event of the widow's remarriage half of the corpus of her trust share was to continue in the trust, but the other half was to be immediately distributed to the remaindermen just named, determined as of the date of the remarriage. (R. 47, 63–65.) (2) The trustees were to pay the income from the second share to the decedent's daughter for life and at her death were to distribute the corpus to her then surviving issue, excepting her son Peter (R. 65). (3) The trustees were to pay the income from the third share to Peter for life and upon his death were to distribute the corpus to his then surviving issue (R. 65–66). Under the Sixteenth Article of the will it was provided that if any trust or part thereof should be held invalid, the corpus of the invalid trust or portion should go outright to the person for whom the equitable life estate had been designated (R. 70).

[2] The ultimate gift over in the absence of surviving issue of the first marriage is not important for present purposes.

By a decree of the Surrogate's Court of New York County entered January 12, 1939, in a proceeding for the judicial settlement of the account of the trustees under the will of Henry H. Rogers, Sr., for the benefit of decedent, it was determined that the trust for Peter and that the trusts as to 6.667 per cent of the shares of the widow and daughter were invalid under New York law. The trusts were otherwise upheld. But the saving clause, the Sixteenth Article of the will, was held to have made outright gifts of one-third of the property to Peter, and 6.667 percent of one-third of the property, in each case, to the widow and to the daughter. The appointment thus did not fail in any respect. (R. 48–49, 92–94.) The value of the 6.667 percent which went outright to the widow and daughter was $187,319.36 as to each (R. 50).

The decedent's widow was 45 years old at the date of his death. She remarried about two years later, on April 30, 1937. Decedent's daughter, Millicent, was 33 years old at the date of his death. (R. 48.) The present worth of a life interest in $1 is $.57143 for a person of 45, and $.67383 for a person of 33 (R. 50).

During the administration of the decedent's estate, his widow filed an application in the Surrogate's Court of Suffolk County for a determination of her right under Section 18 of the Decedent Estate Law to elect to take against the provisions of decedent's will, despite a waiver of her right

of election previously executed and filed with decedent's will. The court dismissed the application on July 13, 1936, and its decision was affirmed on appeal. In a proceeding in the Surrogate's Court of New York County, involving the judicial settlement of the account of the trustees under the will of Henry H. Rogers, Sr., for the benefit of the decedent, his son, Henry H. Rogers III filed an answer attacking the legality of the exercise of the power of appointment. The court held against the son's contentions on May 23, 1938. (R. 48.)

The Commissioner determined by his deficiency notice and contended before the Board of Tax Appeals that the value of the entire property subject to the decedent's exercised power of appointment, of the stipulated worth of $8,428,949.60, should be included in his gross estate for estate-tax purposes. The petitioners contended that the value of the property passing outright to the widow and daughter and the value of the respective trust interests appointed to them should not be included in the decedent's gross estate. (R. 50.) The Board determined that the "value of the property passing to the widow and the daughter under the power was $3,640,122" and that this was less than the value of the property which they would have received as donees in default of appointment. On this basis, the Board excluded so much of the value of the appointed property from the decedent's gross estate, and included only the

value of the balance of the property, stated to be $4,788,837.60. (R. 26.)[3]

On the Commissioner's appeal, the Circuit Court of Appeals reversed the Board and held that the entire value of the property subject to the power of appointment was includible within the decedent's gross estate under section 302 (f) of the Revenue Act of 1926, as "property passing under a general power of appointment exercised by the decedent (1) by will * * *." Although the decision was unanimous, Judges Frank and L. Hand each filed separate opinions and Judge Chase concurred in the result without indicating his individual views (R. 114–118, 119–122).

SUMMARY OF ARGUMENT

I

The decedent, Henry H. Rogers, possessed a *general* power of appointment and *exercised* it. The critical question is whether there was a "passing" of the interests in controversy under the exercise of the power within the meaning of Section 302 (f) of the Revenue Act of 1926, as amended.

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[3] The decedent's property, exclusive of the $8,428,949.60 subject to the power of appointment, was in excess of $14,000,000 (R. 49), and the estate tax liability computed in accordance with the Board's opinion is $7,491,556.07 (R. 38). Subject to final computation, the principal amount of tax involved in this controversy appears to be $1,601,653.68.

It may be noted that the value of the balance of the property covered by the power should be $4,788,827.60, rather than the $4,788,837.60 stated.

Petitioners contend that the value of the interests taken by the widow and the daughter under the exercise of the power was less than the value of the interests which they would have taken in default of appointment, and that therefore there was no passing of the property under the power. The Board of Tax Appeals agreed with this view. Under this point, we accept the valuations of the widow's and daughter's interests determined by the Board. It is our position that there was nevertheless a "passing" of all of the property under the exercise of the power. The court below agreed with our view.

A. We contend, first, that the "passing" requirement simply means that the exercise of the power must be effective, and that it is necessarily effective when the exercise is valid in the first instance and the appointees, as here, fail to renounce.

1. In every practical sense there is a passing of the property in these circumstances, since the appointees rely upon the title provided them under the will of the donee of the power. This is demonstrated in the instant case by the fact that the surrogate's decree was based on the construction, not of the will of the donor of the power, but of the will of the donee, the decedent. The disposition of the property made by decedent's father upon his death in 1909 was merely tentative and was dependent upon decedent's wishes upon his death twenty-six years later. It was decedent's

decision, expressed by his will, which effectively disposed of the property.

2. Section 302 (f), as amended, is derived from Section 402 (e) of the Revenue Act of 1918, which first inserted in the estate tax an express reference to powers of appointment. Neither the statute nor its legislative history furnishes any basis for a distinction based upon the identity of the appointees under the exercise of the power. The pertinent Committee Report strongly supports the conclusion that the framers of the original Section 402 (e) were concerned only with the existence of a general power, which they likened to ownership, and the decision of the donee to assert dominion by exercising the power.

3. Nor is there anything in the general law of powers as it existed in 1918, or exists today, which supports the introduction into the statute of an unexpressed distinction based upon the identity of the appointees. The American cases by strong implication, and the English expressly, take the view that the identity of the appointee is immaterial.

4. Petitioners' theory is that a taker in default acquires a vested interest in the property, subject merely to divestment, and that where a taker in default is left under the exercise of the power with something of what he would have taken in default of appointment there is with respect to that interest no passing under the exercise of the power. Under this view, it is asserted that each case is dependent upon the peculiarities of the local law

as to passing. But the question of whether there is a passing of the property under local law is an artificial one, at best. The result will depend in each case merely on the assumptions which are taken as the starting point of the discussion. It is a question unrelated to the substantial rights and interests of the parties. The question whether the "passing" requirement of Section 302 (f) is satisfied is by its nature wholly a federal question, independent of local law. Cf. *Morgan* v. *Commissioner*, 309 U. S. 78.

5. There is nothing in the administrative application of Section 402 (e) and the succeeding provisions which warrants a distinction based upon the identity of the appointees.

6. *Helvering* v. *Grinnell*, 294 U. S. 153, particularly when read in the light of *Helvering* v. *Safe Deposit Co.*, 316 U. S. 56, confirms the view that the identity of the appointees is of no consequence and that there is a passing of the property under Section 302 (f) when a general power is exercised and the appointees fail to renounce.

7. Under this view, it may be thought that there is somewhat of an incongruity where, unlike the situation in the present case, the beneficiaries and the interests which they receive under the exercise of the power are precisely the same as in default of appointment. If this be an incongruity, it would seem to inhere in the faulty concept of the statute, which fails to tax unexercised powers, a

defect which has since been remedied by the Revenue Act of 1942.

B. If we are wrong in our contention that the failure of the appointees to renounce, without more, requires the application of Section 302 (f), it then becomes necessary to compare the identity of the appointees and their interests with the identity of the takers in default and the interests which they would have taken. Where, as here, the exercise of the power is effective to disturb the flow of benefits, there is a "passing" of all the property, whatever the importance of a failure to renounce.

The *Grinnell* case in this aspect does not support the petitioners' position at all, for it classifies as ineffective only an exercise which fails to disturb the benefits flowing from the will of the donor of the power. Basically, the considerations discussed under A support, *a fortiori,* the proposition that an appointment which changes the economic benefits brings down the tax. Here there was a modification or rearrangement of such benefits to a most substantial degree, for decedent's son, who would have taken one-third outright in default of appointment, was eliminated entirely, decedent's grandson, who would have taken nothing in default, was given one-third outright, and the interests of the widow and daughter were radically modified.

Indeed, the instant case involves such a drastic change in the flow of benefits that the result

reached by the court below can be supported by the somewhat narrower view that, at the least, where the appointment touches every part of the property, and no part can be pointed to as an unaffected remnant of the default interest, the exercise of the power has been completely effective. There was thus a passing of all the property since the interests taken by the widow and daughter were both quantitatively and qualitatively different from what they would have taken in default.

II

We strongly urge that a wholly federal test of "passing" should be applied; the discussion under Point I is independent of local law in this respect. Cf. *Morgan* v. *Commissioner*, 309 U. S. 78. Even if New York law is to be applied, however, the judgment below must be affirmed as to all except the amount of tax attributable to the relatively small share appointed outright to the widow.

A. The New York cases hold that where the *qualitative* interest appointed to a taker in default is different from the interest which would have been taken in default, there is a passing under the exercise of the power. Under this line of cases, all of the property would be included in decedent's gross estate except the two relatively small shares appointed outright to the widow and the daughter.

B. The New York cases also hold that where the interest appointed to a particular individual is of a greater value than that person would have been taken in default, the exercise of the power is wholly effective. This raises the question of the proper value of the interest taken by the daughter. Contrary to the determination of the Board of Tax Appeals, the valuation of her interest must include a value not only for her own life estate but also a value for her contingent right to the corpus of the widow's trust upon the latter's death. When the value of this interest is added to the valuation determined by the Board, it will be seen that the total value of the interest taken by the daughter under the exercise of the power exceeds the value of the one-third share outright which she would have received in default of appointment. Moreover, if the contingency of the widow's remarriage should be taken into account, the value of the daughter's interest would be further increased. Thus, under this second line of New York cases all of the property passing to the daughter must be included within decedent's gross estate.

The view which this Court takes of the case might conceivably make important a factor not heretofore considered, namely, an exact computation of the value of the interest taken by the widow under the appointment. This would raise

questions as to whether the probabilities of her remarriage may be evaluated and, if not, the consequences so far as the valuation of her interest in the one-half of the trust subject to this contingency are concerned. These questions have an importance beyond the instant case, but neither was touched upon in the opinions of the Board of Tax Appeals or of the Circuit Court of Appeals. Accordingly, if an exact valuation of the widow's interest is considered significant, it would be appropriate to remand the case for further proceedings on this point.

ARGUMENT

I

THE ENTIRE VALUE OF THE PROPERTY COVERED BY THE POWER OF APPOINTMENT SHOULD BE INCLUDED IN THE DECEDENT'S GROSS ESTATE

Henry H. Rogers, who died in July 1935, a resident of New York, possessed a power of appointment given him under the will of his father. The applicable statute is Section 302 (f) of the Revenue Act of 1926, as amended by the Revenue Acts of 1932 and 1934 (Appendix, *infra*, p. 61), which provides that the gross estate shall include the value at the time of the decedent's death of all property "passing under a general power of appointment exercised by the decedent (1) by will * * *." The applicable regulations are Treasury Regulations 80 (1937 ed.), Article 24

(Appendix, *infra*, pp. 62–63). It is not disputed that the decedent undertook to exercise the power of appointment; nor is it disputed that *all* of the property actually passed in accordance with that exercise of the power. Petitioners rely principally upon the purported fact that under the exercise of the power decedent's widow and daughter received interests of a lesser value than either would have received in default of appointment. On this basis, petitioners contend that there was no "passing" of these interests to the widow and the daughter under the exercise of the power. Under Point I, we assume the correctness of the Board's determination as to the value of the interests taken by the widow and daughter. It is our position that there was a "passing" of all of the property covered by the power of appointment under the exercise of the power within the meaning of Section 302 (f), as amended.

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[4] The Board apparently arrived at the valuation of $3,640,122 for the interests of the widow and daughter as follows:

"In the case of the widow:	
Value of property passing outright	$187,319.36
Value of interest in trust	1,498,478.32
Total interests taken by widow	$1,685,797.68
In the case of the daughter:	
Value of property passing outright	187,319.36
Value of interest in trust	1,767,004.96
Total interests taken by daughter	$1,954,324.32

The total interests of the widow and daughter so computed equal the Board's total of $3,640,122. This computation accords with petitioners' contentions (Br. 4). In default

Under the will of his father, absent any action on decedent's part, the property covered by the power of appointment would have gone on decedent's death to the latter's widow, son, and daughter outright in equal shares. But decedent, in addition to receiving the income from the property for life, had it within his power to divert the property from the takers in default and to rearrange the distribution as he might choose. Decedent in fact chose to exercise the power, and did so by his will. In consequence, his son was eliminated entirely and a one-third share was given outright to his grandson, Peter, who would have taken nothing in default of appointment. The interests of the widow and daughter, likewise, were radically changed. There was no renunciation by the appointees.

On these facts, it must be agreed that decedent possessed a *general* power of appointment and that he *exercised* it. It is clear, likewise, that

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of appointment the widow and the daughter, respectively, would have taken outright one-third of the property, or $2,809,649.86. Thus, on the Board's computation, each received less under the exercise of the power than she would have received in default of appointment.

It will be observed that the Board failed to add to the value of the daughter's interest the value of her contingent interest in one-half of the widow's share upon the latter's remarriage and in the balance of the widow's share upon the latter's death. The Board likewise failed to reduce the value of the widow's interest by any amount because of the contingency of her remarriage. We discuss these omissions *infra*, pp. 54–60.

there was no renunciation on the part of the appointees and no election on their part to take under the will of the donor. The controversy centers upon the third requirement of the statute, whether there was a *passing* of the property under the exercise of the power.

A. THE APPOINTEES ACTUALLY SUCCEEDED TO THE INTERESTS APPOINTED TO THEM UNDER THE EXERCISE OF THE POWER; THEIR FAILURE TO RENOUNCE THE APPOINTMENT PRECLUDES THEIR CONTENTION THAT THE PROPERTY DID NOT "PASS" UNDER THE POWER

It is our position that the "passing" requirement of the statute is satisfied where there is an *effective* exercise of the power. There must be a general power, it must be exercised, and the passing requirement imports the further condition that the exercise must be effective. Moreover, where, as here, there is an exercise of a general power, it is our position that the failure of the appointees to renounce removes the only obstacle which might have frustrated the effective exercise of the power. Consequently, we submit that the failure to renounce is decisive and demonstrates, without looking further, that there was a passing of the property under the power.

1. Certainly in every practical sense the exercise of the power was wholly effective and there was a "passing" of all of the property under its terms. The direction of the property to the takers in default provided by the will of the donor of the power, decedent's father, upon his

death in 1909, was merely tentative and was dependent upon decedent's wishes at the time of his death twenty-six years later. In the interim the takers in default received nothing from the property and had no salable interest in it. Even if under local property concepts they had assignable interests, it is evident that no purchaser could be found, for their interests could be utterly extinguished or drastically modified by a stroke of decedent's pen. This, in fact, is precisely what happened.

By the Twelfth and Sixteenth Articles of his will, decedent undertook to control at every point the title to all the property. In order to show good title on any subsequent disposition of the property the appointees manifestly would need to rely upon the detailed provisions of decedent's will for the substantiation of their ownership. The terms of the surrogate's decree alone would seem to make argument as to the source of the appointee's title academic. That decree (R. 92–94) is based on a careful examination and construction of the terms of decedent's will, not of the will of his father. Indeed, decedent's son attacked the exercise of the power and was defeated. *Re Rogers*, 168 Misc. 633.[5]

[5] The Board of Tax Appeals held that there was no passing of the interests in controversy, of a value of $3,640,122, under the power of appointment. However, confronted with the practical problem of recounting what had happened, it is

To argue that there is no passing under an exercise of a power of appointment where there *is* a valid exercise and the appointees by failing to renounce *in fact* rely upon it for the title which they take is obviously to contend for a meaning of "passing" at variance with the natural and reasonable understanding of the language used. It is this position which petitioners must maintain.

2. The phraseology of Section 302 (f) of the Revenue Act of 1926, as enacted and as amended, stems directly from Section 402 (e) of the Revenue Act of 1918, c. 18, 40 Stat. 1057, which first brought to the estate tax an express provision as to powers of appointment. In the Committee Report accompanying the original statute there is no emphasis on "passing," as a word of art or otherwise.[6] Probably the expression "passing"

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interesting to note that the Board used the following language (R. 26):

> The value of the property *passing to the widow and the daughter under the power* was $3,640,122. The value of the *remaining property passing under the power* was $4,788,837.60. The $3,640,122 *which went to the widow and daughter under the power* was less than they would have gotten had there been no exercise of the power. [Italics supplied.]

[6] The pertinent paragraph of the Committee Report (H. Rep. No. 767, 65th Cong., 2d Sess., pp. 21–22 (1939–1 Cum Bull. (Part 2) 86, 101) reads as follows:

> There has also been included in the gross estate the value of property passing under a general power of appointment. This amendment as well as that preceding is for the purpose of clarifying rather than

appears in the section only because of the uniform structure of the various subdivisions describing the property includible in the gross estate, and the necessity of connecting "property" with "general power of appointment exercised." "Passing under" had no particular significance but was simply the best connecting phrase that readily occurred.

In this connection it should be borne in mind that, the estate tax being a transfer tax and not an inheritance tax, Congress was imposing an excise upon the exercise by the decedent of his privilege. Thus, it was not concerned with what the appointees of the power received and had no reason to limit the tax to those cases where the appointees profited by the exercise of the power. The scheme of the statute is to levy a tax upon transfers and to base it upon the decedent's interest which ceased upon his death. While Section 302 (f) is confined to exercised powers, it does not

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extending the existing statute. A person having a general power of appointment is, with respect to disposition of the property at his death, in a position not unlike that of its owner. The possessor of the power has full authority to dispose of the property at his death, and there seems to be no reason why the privilege which he exercises should not be taxed in the same degree as other property over which he exercises the same authority. The absence of a provision including property transferred by power of appointment makes it possible, by resorting to the creation of such a power, to effect two transfers of an estate with the payment of only one tax.

551325—43——4

within these limits appear to depart from the statutory plan. Unless petitioners can establish the contrary, the term "passing" in this subsection should be construed as a substitute for the word "transfer" or "transferred." The latter expressions would have been inappropriate in this subsection and probably were not used simply because the decedent never was technically the owner of the property involved in the power. The New York statute (*infra*, p. 31) solved this drafting difficulty by providing that the exercise of a power "shall be deemed a transfer."

In any event, it seems almost certain that the draftsmen of the original Section 402 (e) would not have thought the statute inapplicable because the power happened to be exercised in favor of the donees in default of appointment. The theory, as evidenced by the Committee Report, was that the very possession of a general power of appointment is not unlike ownership, and that the exercise of such a power is an election to assert ownership rights which may be appropriately taxed. The exercised privilege of disposing of property was said to be equally deserving of taxation, whether it derived from actual ownership or possession of such a general power. See *supra*, fn. 6, pp. 20–21. Thus, the draftsmen emphasized the possession and exercise of the power and showed no concern with the identity of the appointees. Indeed, since powers are customary devices in family property

settlements, some or all of the appointees are likely to be the same family members who are described as donees-in-default (although they may not take identical estates or interests), and to have differentiated on account of identity would have largely destroyed the effectiveness of Section 402 (e). Nor, significantly, does the statute or the Committee Report have anything to say of the problems of comparison and evaluation which follow in the wake of the recognition of any such distinction (*infra*, pp. 42–50). An exercise, even though in favor of donees-in-default, was undoubtedly viewed as nonetheless a testamentary act which should be taxed—just as a will is nonetheless a testamentary act because it happens to favor heirs at law.

In short, neither the language of the statute nor its legislative history supports the narrow meaning of "passing" for which petitioners must contend. And no more than in *Detroit Bank* v. *United States*, 317 U. S. 329, 333, is there warrant to "impute to Congress an intention not disclosed by the statute or its legislative history."

3. There is nothing, likewise, in the general law of powers of appointment which persuades that Congress meant to imply an unexpressed distinction based on the identity of the appointees. The traditional view seems to have been that the donee of a power exercises no independent dominion over the property covered by it but serves merely

as the hand of the donor, so that the exercise is read back into the instrument creating the power and the property (in legal contemplation) passes under that instrument. 3 Restatement, Property (1940) 1811–1812; 3 Tiffany, *Real Property* (3d ed.), Sections 680 and 713; see *Wachovia Trust Co.* v. *Doughton*, 272 U. S. 567.[7] Thus, where the power is unexercised, the creditors of the donee are unable to reach the property covered by the power. *United States* v. *Field*, 255 U. S. 257, 264.[8] Nevertheless, these principles, taken at face value, throw no helpful light on the federal statute. To be sure, no tax is imposed under Section 302 (f) with respect to an unexercised power of appointment, and to some indeterminate extent this failure may be attributed to traditional notions of the nature of powers. But no resort to the general law of powers is necessary to determine the existence of this hiatus since Section 302 (f) plainly refers only to "exercised" powers.

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[7] The conclusion of this case concerning a state's power of taxation is no longer good law (*Graves* v. *Schmidlapp*, 315 U. S. 657) but it reflects the traditional conception of powers of appointment.

[8] Even here, however, the difficulties in a black-letter statement of the principles of the law of powers or in the construction by implication of a legislative policy on the basis of such principles are attested by the several states, including New York, which by statute permit creditors of the donee to reach property covered by an *unexercised* power of appointment. As to the New York statute, see *Cutting* v. *Cutting*, 86 N. Y. 522. The states having such statutes are listed in 3 Restatement, Property (1940) 1855–1857.

Cf. *Helvering* v. *Safe Deposit Co.*, 316 U. S. 56, with respect to Section 302 (a). And so far as exercised powers are concerned, the statute as plainly breaks with the traditional view and proceeds on the basis that "the privilege which he exercises" (*supra*, fn. 6, p. 21) properly subjects the donee's estate to the tax.

A majority of the states which have passed upon the point have held that where the power is exercised, the creditors of the donee may reach the property so far as necessary to satisfy their claims. *United States* v. *Field*, 255 U. S. at pp. 262–263. (The cases are collected in 59 A. L. R. 1520, 97 A. L. R. 1071, and 121 A. L. R. 804.)[9] If it is necessary to indulge assumptions, it is perhaps reasonable to suppose that the draftsmen of Section 402 (e) were influenced by the view that the exercise of a power gave the donee a sufficient interest in the property to make it available to his creditors. If so, it is of significance that under the common view the creditors took the property, in these circumstances, without regard to whether the appointment was or was not to takers in default. *Clapp* v. *Ingraham*, 126 Mass. 200, the leading American case holding for the creditors, itself involved an exercise of the power in favor of takers in default, although no point was made

[9] Of course, a strictly logical application of the traditional rule would defeat the creditors even in these circumstances.

of it.[10] It can be said categorically that there was no substantial body of cases which attached importance to the identity of the appointees. Thus, even if the 1918 statute is to be read on this background, there is no basis for importing into the law a differentiation in tax consequences turning on whether the exercise of the power favors takers in default or others.[11]

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[10] In *Hill* v. *Treasurer & Receiver General*, 229 Mass. 474, 476, the rule in favor of creditors is stated to rest "on the fundamental idea that a man ought to pay his debts *when he has the power to do so*, rather than to give property to those who are not his creditors." [Italics supplied.]

[11] The Restatement of the Law of Property (3 Restatement, Property (1940), Section 369) has adopted the view that if the appointment is of the same qualitative interest that the donee-in-default would otherwise have taken, and quantitatively does not exceed what he otherwise would have taken, the property passes not under the power but in default of appointment. The Comments and Illustrations state that the question is important with reference to the rights of creditors of the donee of the power (as to which also see Section 327, Comment b, and Section 329, Comment d), and to the liability of the donee and his heirs for estate and succession taxes.

The Restatement followed by many years the federal statute of 1918 and obviously provides a clue as to the intent of the framers of that statute only to the extent that it adopts rules of law firmly entrenched as of that time. In this connection it should be noted that Section 369 was the subject of a spirited dispute among the reporters and advisers who drafted the Restatement. It is instructive to compare the memorandum for the majority view, prepared by Reporter Leach, with the memorandum of the minority, prepared by Reporter Powell and Adviser Simes (and apparently con-

Moreover, the American case law of powers of appointment is "distinctly thin in quantity," there being virtually no decisions in many states in this field, and as late as the beginning of this century it could be said that there was no such thing as an American law of powers. 3 Restate-

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curred in by Adviser Madden). See Proposed Final Draft No. 2 of the Restatement of Property, 140, 151–155.

The majority brushes aside the many cases turning the rights of creditors solely upon an exercise of the power, with the comment that the issue of appointment to donees-in-default was not there raised. The majority relies upon one Kentucky case (*Boyce* v. *Waller*, 9 Dana 478), which the minority points out to be no longer significant law in Kentucky (since *St. Matthews Bank* v. *De Charette*, 259 Ky. 802, refused to follow the majority rule as to creditors), and one obscure dictum in a Texas Civil Appeals case (*Arnold* v. *Southern Pine Lumber Co.*, 58 Tex. Civ. App. 186, 197). Principally, the majority relies not upon cases which litigated the rights of contesting claimants to property but upon *tax* cases, such as *Re Lansing*, 182 N. Y. 238, and *Helvering* v. *Grinnell*, 294 U. S. 153 (discussed *infra*, pp. 30–32, 34–40).

As the minority observes, it is somewhat strange that a significant provision of the Restatement of the Law of Property should be framed in reliance upon cases interpreting state and federal tax statutes. It is even stranger that the Restatement should attempt to state a rule of federal tax law, such as is attempted by Illustrations 2 and 3 under Section 369. These illustrations are already out of date by virtue of Section 403 of the Revenue Act of 1942, c. 619, 56 Stat. 798, which amended Section 811 (f) of the Internal Revenue Code (U. S. C., Title 26, Sec. 811 (f)), the successor to Section 302 (f).

ment, Property (1940) 1810.[12] This fact furnishes an additional caveat against attempting to read into the federal statute ill-defined concepts of the general law of powers of appointment, which upon more painstaking examination may prove spurious. Still further pause is given by the English cases, which take the view that the exercise of a power immediately divests the estates of those designated to take in default of appointment, and, even if the exercise is in favor of the takers in default, creates a *new* right in them. *In re Brooks' Settlement Trusts,* [1939] Ch. 993. See Farwell, *Powers* (2d ed., 1893) 275–278; 1 Paul, *Federal Estate and Gift Taxation* (1942) 449–451, where the cases are collected and discussed. And it has been assumed in England, as in this country, that a donee's creditors may reach the property even though the appointment is merely to takers in default. See *Vaughan* v. *Vanderstegen,* 2 Drew. 165, 177–178.

4. It is petitioners' theory that the will of the donor gave the takers in default of appointment vested interests in the property, subject merely to divestment on the donee's exercise of the power. Thus, where an exercise of the power is wholly or even partly in favor of the takers in default,

[12] The Restatement adds (pp. 1810–1811) that the—

> number of cases presented to the courts is now rapidly increasing, due largely to the very substantial estate and inheritance tax advantages which often can be obtained by the creation of trusts with powers of appointment.

it is argued that the interest which the default takers receive is merely what is left to them under the will of the donor and that there is no "passing" to them under the exercise of the power. Under this view each case must turn on the peculiarities of local law; it is maintained that under New York property law there is such a vesting under the donor's will.

We discuss *infra*, pp. 50–58, the New York cases relied upon by the petitioners. They fall short of the result which petitioners seek. Our basic challenge, however, goes to the contention that the local law of vesting and divesting is pertinent to the question of "passing." Such questions as whether a power of appointment is created under the will of the donor, the scope of the discretion given the donee, the validity of his exercise of the power and of any subsequent renunciation on the part of the appointees—these, we agree, are properly controlled by local law since they determine the substantial rights and interests of the parties. As applied to these questions it is local law which tells us what has actually happened as a necessary preliminary to the attaching of the tax consequences. But as applied to the question whether the appointed interest "relates back" to the will of the donor of the power and is thus regarded as having been "vested" in the appointee during the interim prior to the appointment, local law adds nothing.

For the answer to this does not touch the fact that it remained wholly within the power of the donee to decide whether the takers in default should ever receive anything of substance, and that by exercising the power the donee has manifested his decision. For present purposes, the relation back, vesting and divesting doctrines would seem to fall into the category of mere labels which a state is free to attach or not as it pleases, but which have no practical consequences and therefore should not be controlling for federal tax purposes. See *Morgan* v. *Commissioner*, 309 U. S. 78;[13] *Lyeth* v. *Hoey*, 305 U. S. 188; *Burnet* v. *Harmel*, 287 U. S. 103.

That the concept of "vesting" and "divesting" is of little practical consequence to the process of actual decision is demonstrated by *Re Lansing*, 182 N. Y. 238, a case which, as we shall see, was relied upon by this Court in *Helvering* v. *Grinnell*, 294 U. S. 153. The *Lansing* case arose under

[13] In the *Morgan* case, holding that what is a "general" power under Section 302 (f) is not controlled by state terminology, this Court stated the controlling principle (pp. 80–81):

> State law creates legal interests and rights. The federal revenue acts designate what interests or rights, so created, shall be taxed. Our duty is to ascertain the meaning of the words used to specify the thing taxed. If it is found in a given case that an interest or right created by local law was the object intended to be taxed, the federal law must prevail no matter what name is given to the interest or right by state law.

New York Laws (1897) c. 284, Section 220, Subdivision 5, which provided that where a power (general or special) is exercised, there—

> shall be deemed a transfer [of the subject property] taxable under the provisions of this act in the same manner as though the property * * * belonged absolutely to the donee of such power and had been bequeathed or devised by such donee by will;[14]

The donor of the power had died prior to the enactment of an inheritance tax law. The donee of the power died afterward but appointed all the property to the person who would have taken in default, and, in addition, the appointee renounced her rights under the will of the donee and elected to take under the will of the donor. The reasoning of the court followed two lines: (1) "The attempt to execute the power was not effective, because it did nothing" (P. 243). (2) The appointee "had the right of election and could refuse to take under the appointment and still hold the property * * *" (P. 244). On these bases it was held, by a divided court, that the tax could not constitutionally apply to the property covered by the power of appointment, since the rights of the appointee derived from the donor and were

[14] It will be observed that the New York statute did not use the word "passing."

unaffected by any action of the donee.[15] But in reaching this conclusion the court did not rely upon the language of vesting and divesting. The early portions of the majority opinion speak of the remainder as having "vested" in the taker in default immediately upon the death of the donor. 182 N. Y. at p. 243. The dissenting opinion, however, strenuously argued that what was taken was not a vested remainder but only a contingent remainder, since the taker could not be determined until the death of the donee. 182 N. Y. at pp. 250–254. Referring to this point of disagreement, the latter parts of the majority opinion abandon the terminology of vested and contingent remainders and insist merely that the rights of the beneficiary had "accrued" on the death of the donor of the power. 182 N. Y. at pp. 248–249.

The inquiry whether by local interpretation there is a "passing" of property under the exercise of a power or under the instrument creating the power is precisely the type of question which has been banned from the interpretation of federal tax statutes by the recent decisions of this Court. *Helvering* v. *Hallock*, 309 U. S. 106; see *Helver-*

[15] Other states differ. *Minot* v. *Treasurer & Receiver General*, 207 Mass. 588; *State* v. *Brooks*, 181 Minn. 262, further hearing, 183 Minn. 251; *Mortague* v. *State*, 163 Wis. 58; *Manning* v. *Board of Tax Commissioners*, 46 R. I. 400. And see Eisenstein, *Powers of Appointment and Estate Taxes: I*, 52 Yale L. J. 296, 322 (1943), for a criticism of the constitutional doctrine of the *Lansing* case.

ing v. *Clifford,* 309 U. S. 331. It is no answer to suggest, as petitioners may, that the statutory use of the expression "passing" compels resort to local law. This assumes the point at issue and returns us to the considerations already discussed, *supra,* pp. 18–32), including the general law of powers at the time the federal statute was adopted. We have found no peculiar significance in the expression "passing" and, as we have seen, no well-grounded distinction turned upon the identity of the appointees where the power was in fact exercised.

5. Nor does anything in the administrative application of Section 402 (c) of the Revenue Act of 1918 or Section 302 (f) of the Revenue Act of 1926 warrant such a distinction. Treasury Regulations 37 (1919 ed.), promulgated within a few months after the enactment of the 1918 statute, contained an express statement (Article 30) that appointed property should be included in the donee's gross estate "although the persons to whom the appointment was made would have taken the property had the power not been exercised." The same provision was continued in Treasury Regulations 37 (1921 ed.), Article 30; Treasury Regulations 63 (1922 ed.), Article 25; and in Treasury Regulations 68 (1924 ed.), Article 24. For no apparent reason, the provision was omitted from Treasury Regulations 70 (1926 ed.), Article 24, and subsequent Regulations. As the cases

thereafter litigated show, the omission was not occasioned by any change in Treasury practice. See Griswold, *Powers of Appointment and the Federal Estate Tax*, 52 Harv. L. Rev. 929, 935, fn. 27 (1939).

6. This brings us to *Helvering* v. *Grinnell*, *supra*, and the subsequent decisions. Like *Re Lansing*, *supra*, the *Grinnell* case involved the exercise of a power of appointment in favor of the takers in default and an effective renunciation of the appointment by the appointees. In consequence, the appointees received under the will of the donor precisely the same interest they would have taken under the exercise of the power. The Court, speaking through Mr. Justice Sutherland, observed that two of the requirements of Section 302 (f) had been met. The decedent possessed a *general* power of appointment and *exercised* it. But it was held that the third requirement was not satisfied because the property did not *pass* under the exercised power.

It will be seen that the precise holding of the *Grinnell* case does not touch the instant controversy, for here there was no renunciation and the interests appointed under the exercise of the power were substantially different from what would have been taken in default of appointment. Discussion of the *Grinnell* case centers upon the apparent rationale of that decision. There is much in the opinion to indicate that the Court

considered the renunciation of the appointment to be of decisive force and that in its absence there would have been a statutory "passing" of the property to the appointees. This was the view of the *Grinnell* case taken in the court below by Judge Frank (R. 114–118).

The core of the *Grinnell* opinion seems to be imbedded in the following language (294 U. S. at p. 155):

> If they [the beneficiaries] had wholly refused to take the property, it could not well be said that the property had passed under the power, for in that event it would not have passed at all. Can it properly be said that because the beneficiaries elected to take the property under a distinct and separate title, the property nevertheless passed under the power? Plainly enough, we think, the answer must be in the negative.

The opinion then goes on to consider in some detail and to approve the reasoning[16] of *Re Lansing, supra*. The discussion of the *Lansing* case concludes with the following quotation from the opinion of the New York Court of Appeals (182 N. Y. at p. 245; 294 U. S. at pp. 157–158):

> An appointee under a power has the right of election, the same as a grantee under a

[16] It seems very clear that the Court regarded the *Lansing* decision as *persuasive* rather than *controlling*—an important distinction so far as the operative force of state law is concerned.

> deed. * * * He can accept the title tendered or reject it in his discretion. It cannot be forced upon him against his will. He cannot be compelled to receive additional evidence of title when he does not want it, and does not need it because his title is perfect without it. His consent is necessary before the attempt to exercise the power becomes binding upon him the same as consent is necessary in making a contract or agreement. Declining or refusing to take has the same effect as incapacity to take, as in the case of a devise to a corporation which has no power to hold any more property because the statutory limit has been exceeded. The title is not affected, but remains where it was before.

The reasoning of the *Lansing* case, however, as we have seen, moved in two directions, and attributed weight both to the fact of renunciation and to the fact that the interest appointed was the exact equivalent of the interest which would have been taken in default of appointment. It must be recognized that the *Grinnell* opinion, in referring to the *Lansing* case, stated both of these grounds of decision. The opinion also contained an earlier quotation from the *Lansing* case (294 U. S. at p. 157), which seems to be directed solely to the point of equivalence.

Moreover, at the end of the *Grinnell* opinion (p. 158) Mr. Justice Sutherland referred to a conflict in "reasoning and conclusions" between

the Circuit Court of Appeals for the Second Circuit in the *Grinnell* case (70 F. 2d 705) and the courts in two cases in which there had been no renunciations (*Wear* v. *Commissioner*, 65 F. 2d 665 (C. C. A. 3d); *Lee* v. *Commissioner*, 57 F. 2d 399 (App. D. C.)). The opinion of the Court continued that "to the extent of the conflict" the "view" of the *Wear* and *Lee* cases was considered to be wrong and that of the court below in the *Grinnell* case to be right. Since the absence of renunciation could have been used to distinguish the *Wear* and *Lee* cases, the failure of the Court to dispose of these cases on this ground gives some support to the view that the renunciation factor was not decisive. But it is not clear that this is the meaning. The *Wear* opinion, reasoning from the legislative history and purpose of the estate tax, had concluded that Section 302 (f) was applicable because the "generating source" of the perfected right of the donees-in-default "was the death of the donee [of the power] without action adverse to them" (65 F. 2d at p. 667). Much the same thought was expressed in the *Lee* case (57 F. 2d at p. 402). The Circuit Court of Appeals for the Second Circuit in the *Grinnell* case had disapproved that argument as proving too much in that it was equally applicable to confirmation of the title of the donees-in-default through *non-exercise* of the power (70 F. 2d 705, 707–708).

In this sense, the reasoning and conclusions of the *Wear* and *Lee* cases were wrong, even though the precise decisions may have been correct. It is not clear that Mr. Justice Sutherland intended to go any further than this.

Though it must be acknowledged that the *Grinnell* opinion mentioned both the factor of renunciation and the factor of lack of any change of interest through the appointment, the recent opinion of the Court in *Helvering* v. *Safe Deposit Co.*, 316 U. S. 56, strongly indicates that the first factor is now considered to be the only significant one. In the *Safe Deposit* case the Court decided that a compromise based in part upon an attempted appointment of very doubtful validity was sufficient to invoke Section 302 (f); the case was remanded with instructions to augment the donee's gross estate by that part of the compromise share going to the appointees which could properly "be imputed to the claim based on the attempted exercise of the power of appointment" (316 U. S. at p. 66). In making its decision the Court used this very significant language (p. 65).

> It is urged that taxes should not be influenced by what occurs after the taxable event; that it is reasonable to consider a compromise *preceding* the receipt of income in connection with an income tax; but that a compromise occurring *after* the decedent's death, which is the "taxable event" under

> an estate tax, should not be considered. Whatever may be the general rule in this respect, this Court has clearly recognized, in *Helvering* v. *Grinnell,* 294 U. S. 153, that events subsequent to the decedent's death, events controlled by his beneficiaries, can determine the inclusion or not of certain assets within the decedent's gross estate under Section 302 (f). In that case, the decedent had exercised a general testamentary power of appointment, an act which under Section 302 (f) brings the property subject to the power within the gross estate. The subsequent renouncement by the appointees of the right to receive by appointment and their election to take as remaindermen in default of appointment were held by this Court to place the property subject to the power outside the scope of Section 302 (f).

This language emphasizes the *exercise* of the power as invoking Section 302 (f), and the renunciation of the appointment as forestalling the application of the section. The plain inference is that, in the absence of renunciation, the tax would have applied in the *Grinnell* situation. Otherwise the reference to the *Grinnell* case in this context is meaningless. The minority opinion in the *Safe Deposit* case seems to agree with this interpretation, observing (316 U. S. at p. 68):

> In *Helvering* v. *Grinnell, supra,* the decedent exercised the power, but the ap-

> pointees, as was their right under state law, elected not to take under the appointment but to take as remaindermen directly from the estate of the creator of the power, and it was held that Section 302 could not be invoked to impose a tax upon the estate of decedent. * * *

The minority opinion then quotes from the *Grinnell* case the language as to the force of an election which we have already quoted, *supra*, p. 35.

Furthermore, the decision in the *Safe Deposit* case conflicts with the notion that there must be a "passing" of the property under the power *according to local law*. The Board of Tax Appeals had held that although the power was purportedly exercised by the donee's will, Section 302 (f) was inapplicable because the donee was too young to make a valid will under the law of his domicile, and hence had not succeeded in passing the property under the law. *Reynolds* v. *Commissioner*, 42 B. T. A. 145. In the Circuit Court of Appeals for the Fourth Circuit and in this Court the Government did not dispute the Board's interpretation of the local law. But this Court took the view that Section 302 (f) applied to the compromise despite the absence of a technical local law "passing" under an exercised power. The question, in the words of Section 302 (f), whether there was a statutory "passing under a general

power of appointment exercised," was regarded as wholly a *federal* question.[17]

7. If we are right in our position, the failure of the instant appointees to renounce is decisive and the tax is applicable without regard to a comparison of the interests taken under the exercise of the power and the interests which would have been taken in default of appointment. It may be thought that this makes for a somewhat incongruous result where the beneficiaries and the interests which they receive under the exercise of the power are precisely the same as in default of appointment. If this be an incongruity it is inherent in the faulty concept of the statute, which fails to tax the nonexercise of powers. See Griswold, *Powers of Appointment and the Federal Estate Tax,* 52 Harv. L. Rev. 929, 935 (1939).

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[17] In *Rothensies* v. *Fidelity-Philadelphia Trust Co.*, 112 F. 2d 758 (C. C. A. 3d), and *Legg's Estate* v. *Commissioner*, 114 F. 2d 760 (C. C. A. 4th), decided prior to the *Safe Deposit* case, the courts interpreted the *Grinnell* decision to mean that failure to renounce was indecisive and undertook to decide whether there was a "passing" of the property under the exercise of the power according to the local law (that of Pennsylvania). The same interpretation of the *Grinnell* case was recently reaffirmed by the Circuit Court of Appeals for the Third Circuit in *Lewis* v. *Rothensies*, decided September 1, 1943. In each case decision went for the taxpayer. For the reasons already discussed, these cases were wrongly decided. They also seem erroneous for another reason (discussed under Point I B, *infra*, pp. 42–50) in that in none was there an equivalence between the interests appointed under the power and the interests which would have been taken in default of appointment.

And this defect has now been corrected by Section 403 of the Revenue Act of 1942, c. 619, 56 Stat. 798, under which possession rather than the exercise of powers of appointment is the significant consideration.[18]

B. WHERE, AS HERE, THE EXERCISE OF THE POWER IS EFFECTIVE TO DISTURB THE FLOW OF BENEFITS, THERE IS A PASSING OF ALL THE PROPERTY UNDER THE POWER

If we are wrong in our position that the failure of the appointees to renounce the appointment requires, without more, the application of Section 302 (f), it then becomes necessary to compare the identity of the appointees and their interests with the identity of the takers in default under the will of the donor and the interests which they would have taken. For example, it is not disputed in this case that the one-third interest taken outright by Peter, who was not a taker in default, must be included within decedent's gross estate. Similarly, it is not disputed that the interests appointed to follow the trust estates of the widow and the daughter must be included within the gross estate. As under Point I A, *supra*, it is our position that, in addition, the interests taken out-

[18] In this connection, it should be noted that taxpayer's comments on Section 403 of the Revenue Act of 1942 (Br. [illegible]) are based upon a theory of a partial release of a general power, leaving only a restricted power to be exercised by will. Whether such a partial release would be valid is arguable, and whether decedent, in any event, would have chosen during his life so to restrict his exercise of the power at death is wholly speculative.

right and the trust estates appointed to the widow and the daughter must be included. We submit that any exercise of a power which is effective to disturb the flow of benefits, either with respect to the identity of the beneficiaries or of the interests taken, works a "passing" of all the property under the power.

It should be noted, at the outset, that in this aspect the *Grinnell* case can give petitioners no support whatever. The *Grinnell* opinion, relying upon the *Lansing* case, classifies as ineffective only an exercise "which leaves everything as it was before" (294 U. S. at p. 157). The exercise in the *Grinnell* case, like that in the *Lansing* case, made absolutely no change in the flow of economic benefits. It bestowed the same quantitative and qualitative interests upon the same appointees who would have taken in default of appointment, a consideration that may be regarded as critical in the light of *Re Cooksey*, 182 N. Y. 92, argued on the same day as the *Lansing* case, and *Re Dows*, 167 N. Y. 227 (affirmed *sub nom. Orr* v. *Gilman*, 183 U. S. 278), both of which were distinguished in the *Lansing* opinion (182 N. Y. at pp. 246–247). In these cases the appointments were to the donees in default, but with slight variations in the time and manner of payment. They were held to be effective appointments, incurring the New York tax. Thus, the careful description in the *Lansing* opinion of effective appointments as those which leave everything absolutely unchanged was sig-

nificant, and it is fair to assume that the significance was not lost on this Court. Assuming, then, that the failure to renounce is not alone decisive, the strong implication of the *Grinnell* case is that an exercise of a power which fails to leave everything as it was before and which accordingly does disturb the flow of benefits is effective to render the tax applicable.

The facts of the instant case show that here to a very substantial degree there was a modification or rearrangement of the flow of benefits. Not only was Henry Rogers III, who under the will of the donor would have taken a one-third share outright, eliminated entirely, in favor of the grandson, Peter, who would not have taken in default of appointment, but the interests of the widow and daughter were also radically changed. Under the will of the donor, they would have each received one-third of the property outright. In fact, they each received outright only a minor share. The balance of the property was conveyed not to them individually, as contemplated by the donor's will, but to trustees who were complete strangers to the donor's will. It was the latter who received legal title and assumed the rights and obligations of legal ownership. Apart from the contingent interest given the daughter in the widow's share, the widow and daughter, respectively, were given only choses-in-action against the trustees to compel them to pay over the income to them, and this only during specified

periods. The decedent exercised his power over the property to terminate one-half of his widow's interest in the trust upon her remarriage (which occurred within two years after his death) and to direct the disposition of all of the remaining trust property upon the death of the widow and the daughter, respectively.

Indeed, the present case presents so thoroughgoing a rearrangement of the interests that the decision below can be supported without the necessity of approving the rule that *any* change in the flow of benefits is sufficient to incur the tax. In the court below, Judge L. Hand found it unnecessary to approve "the absolute doctrine that in the absence of renunciation all interests appointed must inevitably pass under the power" (R. 122). He also found it unnecessary to hold that *any* modification of the flow of benefits was sufficient to require a passing of the property under the power, and assumed "for argument" (R. 120) that there might be a passing of some interests under the power but not of others. He did accept, however, our further alternative position that where every part of the subject property is affected by the appointment—that is, where there is no part which can be pointed to as an untouched remnant of the default interest which would have passed absent appointment—then the exercise of the power has been completely effective. In Judge Hand's words, "no interests should be excluded from the donee's estate to whose creation

the exercise of the power was necessary" (R. 120). Even under this restricted test, which we likewise urge as an alternative contention here, it will be seen that every part of the property did pass under the appointment.

From a quantitative standpoint, overlooking the qualitative differences in the interests appointed to the widow and the daughter, the decisive fact is that the decedent appointed one-third of the property to Peter, who was not named in the donor's will. Once this had been decided upon, it was impossible for the decedent to permit the remainder of the property to pass in default without frustrating his purpose with respect to the widow and the daughter. Had the balance passed in default, the widow and daughter would have shared equally with Henry Rogers III in the remaining two-thirds and would have received only two-ninths of the property, respectively. As Judge Hand observed (R. 121), in order to give to each the widow and the daughter even legal interests in one-third of the property, it was absolutely essential for the decedent to exercise his power with respect to them.

Also important is the change in the quality of the interests which was effected by the exercise of the power.[19] Plainly, there was no way in which

[19] Judge Hand observed (R. 121) that the distinction between legal and equitable interests is important under New York law. In this connection, it should be noted that he referred to the state law only for light on the nature of the interests created, and not on the question of "passing."

decedent could have secured the conveyance of the property to trustees for the benefit of the widow and the daughter, rather than a conveyance to them outright, without exercising the power with respect to their shares. Similarly, there was no way in which he could have terminated the widow's interest in a part of the corpus upon her remarriage and the balance of her interest upon her death, or the daughter's interest upon her death, or have appointed contingent interests following the termination of the trust estates, without exercising the power.

It is petitioners' contention that where a power is exercised in such manner as to appoint to the same beneficiary an interest of less value than he would have taken in default of appointment, the exercise of the power *pro tanto* is ineffective and no property passes under it. It will be seen, however, that this view is wholly artificial and depends upon a series of assumptions constructed to secure the desired result. In the present case the monetary value of the property taken outright and of the trust interests of the widow and the daughter was less than the one-third interests which they would have taken in default of appointment. But it is indulging in fiction to say that these interests resulted, not from an exercise of the power with respect to the widow and daughter, but merely from appointing away to others various interests in the property. As we have seen, the appointment to Peter would not have se-

cured the results which accrued, even overlooking the qualitative differences in the interests in fact taken by the widow and the daughter; it was necessary for the decedent to go further and to make an express disposition of the balance of the property. So likewise with respect to the qualitative differences. By no conceivable method of carving away remnants of the property could decedent have caused the untouched balance to wind up in the hands of the Central Hanover Bank and Trust Company and two individuals as trustees for the widow and daughter. It does not seem logically possible to say, for that matter, that a life estate even absent a trust is merely an undisposed of portion of a fee interest. And it becomes even more fanciful to suggest that a contingent interest could in any circumstances represent an undisposed of remnant of a fee.[20]

It is true that *Rothensies* v. *Fidelity-Philadelphia Trust Co.*, 112 F. 2d 758 (C. C. A. 3d), and *Legg's Estate* v. *Commissioner*, 114 F. 2d 760 (C. C. A. 4th), held that an equitable life estate is a remnant which can be obtained by starting with an absolute interest and carving away portions of it. This result was obtained upon a pur-

[20] Even the Restatement, which takes the position that nothing passes under the exercise of a power when the appointed interest is quantitatively of equal or less value than that which would have been taken by the same person in default of appointment, is silent where the interests are qualitatively different. 3 Restatement, Property (1940), Section 369, Second Caveat.

ported application of Pennsylvania property law, which is at best doubtful upon the basis of the two Pennsylvania cases relied upon.[21] However, the law of New York is to the contrary where qualitative differences are concerned (*infra*, pp. 51–53) and even if the Pennsylvania cases supported these decisions, it seems clear that the application of a federal taxing statute should not be shaped to such local peculiarities.

We submit, therefore, that even if the failure of the beneficiaries to renounce was not decisive, petitioners must still fail. Without regard to the state law of vesting and divesting, there is a "passing" of the property under Section 302 (f) where the exercise of the power is effective to disturb the flow of benefits. At the very minimum, there is a passing of the property under the exercise of the power where there is no untouched remnant which goes to a taker in default. In the language

[21] The Third and Fourth Circuit cases relied upon *Freeman's Estate* (*No. 1*), 35 Pa. Super. Ct. 185, and *Potter's Estate*, 13 Pa. Dist. & Co. R. 667. *Freeman's Estate* involved a gift of trust income to A's children for the specified duration of the trust, unless A otherwise appointed. A appointed the income to his wife for life, with no other appointment. It was held that his children had a vested interest which was only partially defeated by the appointment, i. e., the children took the income after the wife's death.

Potter's Estate was decided for the purpose of saving federal taxes, and apparently for no other purpose. No substantive rights appear to have been affected. The gift in default was identical with the appointed gift in both quantity and quality, and the court for that reason concluded that the property passed under the donor's will.

of Judge Hand, "no interests should be excluded from the donee's estate to whose creation the exercise of the power was necessary" (*supra*, p. 45). Under any of these tests the exercise was completely effective in the instant case and there was a passing of all of the property under it.

II

Even Applying New York Law, All of the Property Must be Included Within Decedent's Gross Estate Except One Small Share Appointed Outright to the Widow

The discussion under Point I, A, and B, is independent of the peculiarities of local law regarding the passing of property and contends for a wholly federal test with respect to the application of Section 302 (f). If either of the alternative views advanced under A or B is accepted by the Court, further discussion will be unnecessary. If the Court should disagree, however, with the substance of what has been said under Point I, we then desire to press certain further considerations in support of the decision below. It is our position that even the New York cases purporting to decide when a power of appointment has been effectively exercised, and thus by analogy when there has been a passing of property under it, require affirmance of the judgment below as to all except the amount of tax attributable to the rela-

tively small share appointed outright to the widow, of a value of $187,319.36."

A. Whatever the New York law as to the effect of powers of appointment where the *quantitative* interest is equal to or less than the interest which would have passed to the same beneficiary in default of appointment, it seems reasonably well established in the state tax cases that where the *qualitative* interest appointed to a taker in default is different from what would have been taken in default of appointment, there is a passing under the exercise of the power. *Re Cooksey*, 182 N. Y. 92; *Re Dows*, 167 N. Y. 227, affirmed *sub nom. Orr* v. *Gilman*, 183 U. S. 278; *Re Rogers*, 71 App. Div. 461, affirmed, 172 N. Y. 617; *Re Warren*, 62 Misc. 444; *Re Lowndes*, 60 Misc. 506. Cf. *Re Rynear*, 130 Misc. 804; *Re Chapman*, 133 App. Div. 337. Also, see *Re King*, 217 N. Y. 358, *Re Canda*, 197 App. Div. 597 (see p. 600), applying the *Lansing* principle, involved an appointment of equitable life estates to the donees-in-default but the nature of the interests which they would otherwise have taken is not revealed; and,

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[11] In attempting to prove that the New York decisions support their position, the petitioners are forced to rely upon state tax decisions, rather than upon decisions adjudicating the property interests of private litigants. It seems evident that state tax cases are a poor vehicle for the determination of property law, since they involve public interests which rightly tend to obscure the precise distinctions which may be appropriate in adjudicating claims between individuals. Cf. *Re Lansing*, *supra*.

in any event, the appointees elected to reject the appointments and to take in default.[23]

Re Lichtenstein, 177 Misc. 320, is contrary to the great weight of authority and holds that an appointed interest of different quality may nevertheless pass under the will of the donor. The court said (p. 326) that the answer was "not clear under the cases in this State" but had been settled by the federal cases, referring to *Legg's Estate* v. *Commissioner, supra,* and *Rothensies* v. *Fidelity-Philadelphia Trust Co., supra.* We submit that no weight should be attached to a decision of an inferior court which is against the mass of authority in its own jurisdiction, and which relies upon federal cases in turn dependent upon the law of another jurisdiction. To argue that cases of very considerable consequence to the federal revenue should turn on a lower state

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[23] At the time this case was decided the factor of renunciation was considered significant, under *Re Slosson*, 216 N. Y. 79. *Re Duryea*, 277 N. Y. 310, which indicates that election is no longer important, had not yet been decided.

Possibly some of the above-cited cases, such as *Re Cooksey, supra,* could have been made to turn on the point that the interests appointed were quantitatively greater than what would have been taken in default of appointment. (See cases cited *infra*, pp. 53–54.) The fact is that none of the cited cases appears to have been decided on that basis.

Re Dows, supra, and *Re Lowndes, supra,* were proceedings to fix the tax with respect to the estate of the donor of the power rather than of the donee. But the question was the same as though the tax were sought to be collected from the donee's estate, namely, whether the power had been effectively exercised.

court decision of this character underscores the impracticality of the state-law approach to the problem.

Apart from the small shares appointed outright to the widow and the daughter, the quality of the interests which they took under the power of appointment was obviously different from the interests which they would have taken under the will of decedent's father. Under the will of the latter, they would, of course, have taken the entire balance of the one-third shares in fee. Under the exercise of the power, they received equitable interests in the balance of the one-third shares for specified periods, and the daughter, in addition, received merely a contingent interest in the widow's share. Under the foregoing line of New York cases, therefore, the exercise of the power was effective as to all of the property in controversy except the two shares appointed outright to the widow and the daughter, of a value in each case of $187,319.36.

B. It is also apparently settled by the New York tax cases that where under the exercise of the power the appointee receives an interest of greater value than he would have received in default of appointment, the exercise of the power is wholly effective. *Re Delano,* 176 N. Y. 486, affirmed *sub nom. Chanler* v. *Kelsey,* 205 U. S. 466; *Re King, supra; Re Taylor,* 209 App. Div. 299, affirmed, 239 N. Y. 582; *Re Vanderbilt,* 281 N. Y. 297, affirmed *sub nom. Whitney* v. *Tax Com-*

mission, 309 U. S. 530; *Re Chauncey*, 102 Misc. 378. Cf. *Re Vanderbilt*, 50 App. Div. 246, affirmed, 163 N. Y. 597.

This line of cases raises the question of the proper valuation of the daughter's interests. Petitioners have contended only that the value of the property appointed outright to the widow and the daughter and the value of their interests in the trust estates should be excluded from decedent's gross estate (R. 50).[24] In taking this position they were perhaps apprehensive of the application of the New York cases last cited. The Board of Tax Appeals, in accord with petitioners' contentions, computed the value of the interests passing to the widow and the daughter in a manner to include only the value of the property passing outright and of their interests in the trust estates. (And in valuing the interest of the widow in the trust estate, the Board made no deduction on account of the contingency of her remarriage. See

[24] It will be noted that the stipulation (R. 50), in stating petitioners' contention, refers to the interests of the widow and daughter in the trust estates as "life interests." The interest of the widow, of course, was not a life interest in the entire corpus of her share of the trust, since the trust in one-half of the corpus was to terminate upon her remarriage. To avoid confusion, we have throughout the brief referred to the widow's and daughter's alleged "life interests" in the trusts simply as their interests in the trusts, without regard to the provision as to the widow's remarriage. Either terminology refers only to the interests of the widow and daughter as income beneficiaries of the trusts and does not include the daughter's contingent interest in the corpus of the widow's trust (*supra*, fn. 1, p. 3).

pp. 58–60, *infra.*) On this basis, the Board reached a value for the excluded property of $3,640,122, apparently computing the total value of the daughter's interests at $1,954,324.32 (*supra*, fn. 4, p. 16). It seems clear that this valuation is too low, since it fails to take into account the value of the daughter's contingent interest in the corpus of the widow's trust. While petitioners have made no contention regarding this interest, it should be included if the New York cases are to apply since under them it is important to determine whether the interests appointed exceed in value the interests which would have been taken in default of appointment.

Under the decedent's will the trustees, upon the remarriage of decedent's widow, were to pay over one-half of her share of the trust corpus (R. 64)—

> to the issue of my marriage with my wife Pauline surviving such remarriage, in equal shares, per stirpes and not per capita, absolutely and forever. In the event that no issue of my marriage with my wife Pauline shall survive the date of her remarriage, I give, devise and bequeath said one-half of the principal of the trust estate to my other issue surviving the date of her remarriage, except Henry, per stirpes and not per capita, or if no such other issue of mine, except Henry, survive the date of such remarriage, then to my heirs at law and next of kin, except Henry, entitled to inherit the same under the laws of the State of New

York in force upon the date of such remarriage.

In the event of such remarriage, the remaining portion of the widow's trust share was upon her death to be paid over absolutely to the remaindermen just named, determined as of the date of the widow's death. Likewise, in the event the widow never remarried, all of her share of the trust property was to be paid over absolutely upon her death to these remaindermen, determined as of the date of her death. (R. 63–64.) As we have seen, there were no children of decedent's marriage with the widow, and there were only two others of decedent's children, Millicent and Henry, surviving his death. Henry and his issue were excluded, however, from participation in the distribution of the corpus of the widow's trust, leaving Millicent alone or her issue as participants.[25] It is on this

[25] We do not believe that the children of Henry, if there were any, could take under a gift over to decedent's "issue * * *, except Henry, per stirpes and not per capita," and we mention the point only because petitioners contended otherwise in the court below. "Per stirpes" means representation according to stock. The issue of any child deceased at the determinative date would, under a limitation to issue per stirpes, take only the share which their deceased ancestor would have taken if he had lived until that date. 3 Page on *Wills* (Lifetime Ed.), Sec. 1070. See *Re Wienholz*, 94 Misc. 55; *Re Foster*, 144 Misc. 622, 625. For specific applications of this rule excluding the issue of an ancestor who had been disinherited, see *Sullivan* v. *Straus*, 161 Pa. 145; *Power* v. *Power*, 296 Ill. 611; *Maddock* v. *Haines*, 88 F. 2d 350 (C. C. A. 7th). Under

basis that the value of Millicent's interest at the date of decedent's death in the corpus of the widow's trust must be determined.

The present worth of $1 due at the death of a person aged 45 (the widow) provided a person now aged 33 (the daughter) is then living is $.32983.[26] Applying the factor of $.32983 to the value of the property put in trust for the widow ($2,622,330.50)[27] the product is $864,923.27. When this amount is added to the value of the interests of the daughter in her share of the property taken outright and in the trust estate created for her benefit ($1,954,324.32), it will be seen that the total value of the interests taken by the daughter amounts to $2,819,247.59. This exceeds the value ($2,809,649.86) of the one-third share which the

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the above authority, the Fifteenth Article of decedent's will (R. 69–70) would appear to have no bearing on the matter. See *Re Weissmann*, 137 Misc. 113, affirmed, 232 App. Div. 698.

[26] This factor is based on the Actuaries' or Combined Experience Table of Mortality, with compound interest at the rate of four percent a year, as is required by Treasury Regulations 80 (1937 ed.), Article 10 (i) (3), and the results set forth above are taken from computations made by the Bureau of Internal Revenue. Of course, if the court agrees with the Government's position here, it would be appropriate to remand the case so that the figures and computations may be checked under proper safeguards.

[27] This figure is obtained by deducting from the value of one-third of the entire property ($2,809,649.86) the value of the interest taken by the widow outright ($187,319.36).

daughter would have taken outright in default of appointment. Moreover, this computation does not take into account the fact that the daughter's interest in one-half of the corpus of the widow's trust was to pass immediately to the daughter in event of the widow's remarriage. We refer to this factor, *infra*, pp. 58–60. If this contingency is taken into account, the value of the interests appointed to the daughter is increased and would exceed by a wider margin the value of the one-third share which she would have received outright in default of appointment.

Applying the line of New York cases applicable where the interest appointed exceeds the value of the interest which would have been taken by the same beneficiary in default of appointment, it thus appears that the exercise of the power was effective as to the entire interests taken by the daughter, including even the share appointed outright, and that all should be included as a part of decedent's gross estate.

Consequently, the net effect of an application of New York law is to exclude from decedent's gross estate only the small share appointed to the widow outright.

The ultimate view of the case which the Court adopts might conceivably make important an exact computation of the value of the interest received

by the widow under the appointment.[28] As we have seen (*supra*, pp. 54–55), the Board of Tax Appeals computed the value of the widow's share under the exercise of the power as if she had a life interest in the trust established for her benefit, without regard to the contingency of her remarriage. (Similarly, the Board placed no value upon the daughter's contingent interest in the corpus of the widow's trust, and hence for this purpose did not take into account the factor of the widow's possible remarriage.) The fact is, however, that in the event of the widow's remarriage one-half of the corpus of the trust established for her benefit was to be paid over to the daughter. If a precise valuation of the widow's interest becomes important, questions arise (1) whether the probabilities of the widow's remarriage may be evaluated (compare *Humes* v. *United States*, 276 U. S. 487, and *Robinette* v. *Helvering*, 318 U. S. 184, with *Brotherhood* v. *Pinkston*, 293 U. S. 96, and *Commissioner* v. *State Street Trust Co.*, 124 F. (2d) 948 (C. C. A. 1st); and (2) whether, if they may not be evaluated, the consequence is (a)

[28] Such a situation would arise, for example, if the Court should reject our argument under Point I *in toto* and accept our argument under Point II only to the extent of agreeing that all of the daughter's interest passed under the power because it was of a greater value than the interest which she would have taken in default of appointment. The result would be that the widow's interest, which obviously was of less value than the one-third she would have received outright in default, would be excluded from the gross estate.

that the contingency should be ignored and the widow's interest in the entire trust treated as a full life interest, or (b) that the value of her interest in the one-half of the trust subject to the contingency should be wholly eliminated (cf. *Helvering* v. *Fitch*, 309 U. S. 149; *Helvering* v. *Leonard*, 310 U. S. 80; *Pearce* v. *Commissioner*, 315 U. S. 543, and *Robinette* v. *Helvering*, *supra*). Neither question was considered by either the Board of Tax Appeals or the Circuit Court of Appeals in their opinions disposing of this case, and in view of the collateral character of these questions, it would be appropriate to remand the case for further proceedings if the precise value of the widow's interest be deemed material.

CONCLUSION

The judgment of the court below should be affirmed.

Respectfully submitted.

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APPENDIX

Revenue Act of 1926, c. 27, 44 Stat. 9:

SEC. 302 [as amended by Section 404 of the Revenue Act of 1934, c. 277, 48 Stat. 680]. The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside the United States—

* * * * *

(f) [as amended by Section 803 (b) of the Revenue Act of 1932, c. 209, 47 Stat. 169]. To the extent of any property passing under a general power of appointment exercised by the decedent (1) by will, or (2) by deed executed in contemplation of or intended to take effect in possession or enjoyment at or after his death, or (3) by deed under which he has retained for his life or any period not ascertainable without reference to his death or for any period which does not in fact end before his death (A) the possession or enjoyment of, or the right to the income from, the property, or (B) the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income therefrom; except in case of a bona fide sale for an adequate and full consideration in money or money's worth; and

* * * * *

Treasury Regulations 80 (1937 ed.):

ART. 24. *Property passing under general power of appointment.*—Property passing under a general power of appointment must be included in the gross estate of the person exercising the power (known as the donee, or appointor), if the power is exercised by will. It should be so included if the power is exercised by deed or other instrument in contemplation of death. It should also be so included if the power is exercised by deed or other instrument with the intent that the transfer shall take effect in possession or enjoyment at or after the death of the donee of the power. (For description of transfers made in contemplation of death and transfers included in the phrase, "intended to take effect in possession or enjoyment at or after * * * death," and the taxability thereof with reference to when made and when the death occurred, see articles 16, 17, 18, and 19.) The statute, however, does not require inclusion in the gross estate of the appointed property in the case of a bona fide sale thereof by the donee of the power for an adequate and full consideration in money or money's worth.

Only property passing under a general power should be included. Ordinarily a general power is one to appoint to any person or persons in the discretion of the donee of the power, or, however limited as to the persons or objects in whose favor the appointment may be made, is exercisable in favor of the donee, his estate, or his creditors. Duplicate copies of the instrument granting the power and of the instrument by which the power was exercised, one of

each to be certified or verified, must be filed with Form 706 in all cases, unless the decedent was a nonresident, in which case only one copy of each instrument, certified or verified, is required.

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